EDMONTON

2002 Investment Committee ANNUAL REPORT

Overview

All of the world's major equity markets posted negative returns for 2002. This is the first time since the 1930s Great Depression that equity markets have had three consecutive years of negative returns.

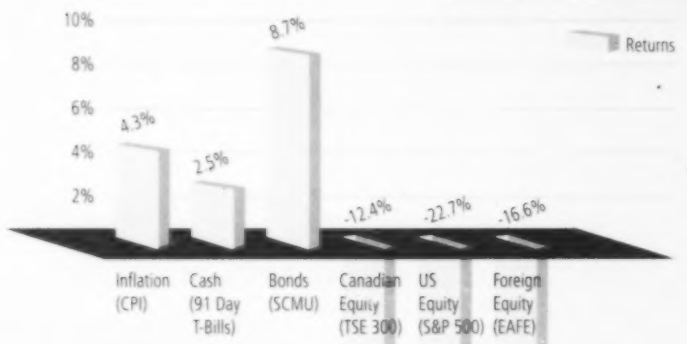
Capital markets have struggled with a continued economic overhang from the bursting of the 'technology bubble', geo-political events, fraudulent financial reporting and corporate governance scandals.

The expectation going forward is that equity markets will improve in the near term and that the historic relationship between equities and fixed income (bonds) will re-emerge but with a smaller equity premium than was experienced in the 1990s.

The City of Edmonton's investment funds experienced a wide range of results depending on each fund's policy asset allocation between equities and fixed income. The best performing fund was the Sinking Fund (made up entirely of fixed income instruments – long term bonds), earning a 10.6% rate of return. The worst performing fund was the Ed Tel Endowment Fund, which lost 4.4% in 2002.

The most significant determinant of investment performance continues to be the asset mix decision, the percentage allocation to equities and fixed income. The asset allocation policies for the City's funds have been established to meet the specific objectives for each fund and the Investment Committee continues to believe that the asset allocation policies are appropriate.

2002 Capital Market Returns



Asset Mix

- The composition of an investment fund between the different asset classes is the "asset mix."
- For example, a fund could have a policy asset mix of 5% cash, 35% bonds, 30% Canadian equity and 30% global equity.
- The "policy asset mix" is the long term target asset mix of the fund, as stated in the Investment Policy. This mix, over a long period of time, should allow the fund to meet its explicitly stated "investment objectives." Over shorter time periods the returns may fall short or exceed the investment objectives.

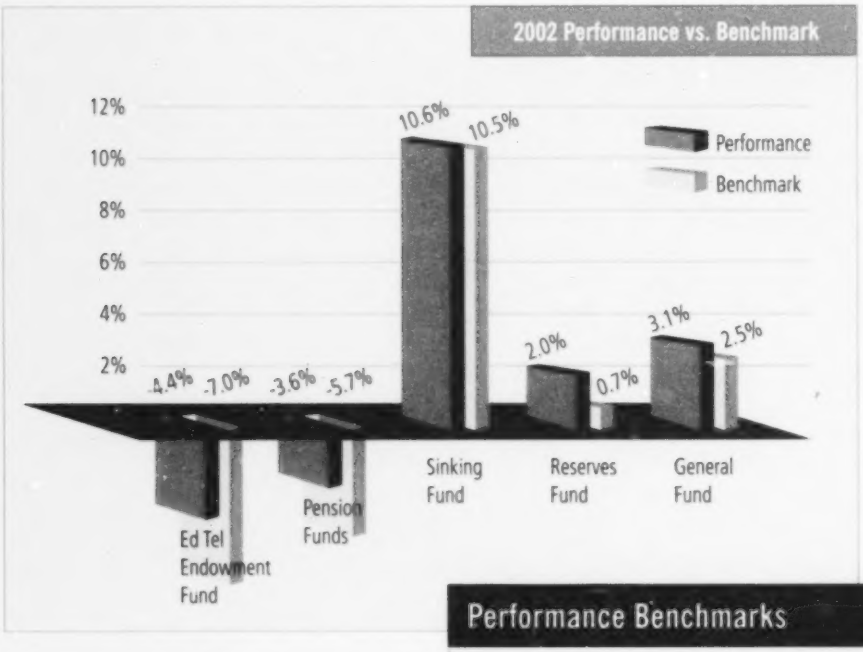
Performance

All of the funds monitored by the Investment Committee outperformed their policy benchmarks for the calendar year 2002. On the more important four-year basis, all of the funds outperformed their benchmarks with the exception of the Sinking Fund.

Comparing the performance to the policy benchmark is the standard way to evaluate the effectiveness of an investment program like the City's. Unfortunately, outperformance vs. the benchmarks doesn't pay dividends or pension benefits when the absolute returns (variance from zero) are negative. Over longer time periods, the funds have done well on both an absolute and relative basis. The Pension Fund has earned a rate of return of 9.4% per annum for the 10 years ending December 31, 2002 compared to the benchmark return of 8.7% per annum.

Since its inception in 1995, the Ed Tel Endowment Fund has earned an annualized (compound annual) rate of return of 9.0% vs. the benchmark return of 7.5%. This has allowed the fund principal to grow from $465 million to $561 million and for the fund to pay $268 million in dividends to City operations.

The Investment Committee continues to believe that over the long term equities will outperform bonds. However, since equity returns are more volatile than fixed income (bonds) returns, equity investments are only suited for investment portfolios with long investment horizons. Consistent with this, only funds with long investment horizons (Ed Tel Endowment Fund and the Pension Fund) have significant equity allocations. Conversely, the investment funds with shorter time horizons (working capital funds) are not invested in equities and accordingly were sheltered from the short term underperformance of the equity markets.



2002 Highlights

2002 was a year for the Investment Committee to focus on monitoring and evaluating the investment program after making significant changes in 2001.

Some of the specific projects undertaken in 2002 include:

- Completing a review and update of performance measurement reporting so as to include new benchmarks, investment managers and asset allocations. The review also determined the best way to use the performance measurement information to evaluate investment managers and strategic investment decisions.
- Developing a process to systematically re-balance the asset mix of the funds. Re-balancing is required to keep the ratio of equities and fixed income compliant with the policy asset allocations. The study reviewed various methods of re-balancing and established a process that is consistent with industry best practices.
- Completing a Council-directed assessment of the risks to the City's investment portfolio. The assessment was completed with the assistance of Scotia Capital Inc. and Mercer Investment Consulting Ltd. The assessment focused on all assets held for the purpose of generating an income stream for the City. This includes the Ed Tel Endowment Fund, the Reserves Fund and the Energy Division of EPCOR Utilities Inc. Assets

Performance Benchmarks

- A benchmark is a "return target comparison" used to evaluate the effectiveness of an investment program.
- The following are the specific asset class benchmarks referred to throughout this report:
  Short Term (Cash): Scotia Capital Markets 91 Day Treasury Bill Index (91 day t-bill)
  Bonds: Scotia Capital Markets Universe Bond Index (SCMU)
  Canadian Equities: Toronto Stock Exchange 300, Nesbitt Burns Capped 10%, Total Return Index (TSE 300, Capped 10%)
  US Equities: Standard & Poors 500 (S&P 500)
  Foreign Equities: Morgan Stanley Capital Inc. Europe, Austral-Asia, Far East Index (MSCI EAFE)
  Global Equities: Morgan Stanley Capital Inc. World Index (MSCI World)
- The "total fund benchmark" consists of the above indices weighted by the policy asset mix. This is used for evaluating the investment performance of the "Total Fund."

owned for the purpose of providing municipal services were not included in the risk assessment. The key findings of the assessment, with respect to the Ed Tel Endowment and Reserves Funds, were as follows:

1. That the current dividend payout for the Ed Tel Endowment Fund is unsustainable. The annual dividend must be reduced and/or the policy of inflation indexing the dividend and principal must be revisited.
2. Introducing a smoothing mechanism to the Ed Tel Endowment Fund dividend could provide for a more stable and predictable dividend payment.
3. The asset mixes for the Ed Tel Endowment Fund and the Reserves Fund are very efficient (risk/return relationship), however some fine-tuning may be appropriate.

Endowment Fund Terminology

Nominal Rate of Return: The rate of return earned by an investment fund without considering the effect of inflation on the value of the earnings. (Example: The fund earned a rate of return of 7.5% in 2002.)

Real Rate of Return: The rate of return earned by an investment fund adjusted for the rate of inflation. (Example: The fund earned a nominal rate of return of 7.5%, the rate of inflation was 2.5%, and therefore the real rate of return was 5%.)

Payout Ratio: The percentage of an endowment fund that is paid out annually as dividends or grants. (Example: A $100 million endowment fund with a 5% payout ratio will provide $5 million annually in dividends or grants.)

Smoothing Mechanism: A technique used by endowment and pension plans to smooth out the effects of volatile investment returns on dividends and contribution rates.

The Future

The Investment Committee will monitor several key projects in 2003.

- Completing an asset mix study for the long-term disability (LTD) plans that began last fall.
- Reviewing the asset mix of the Fire Fighter's Supplementary Pension Plan.
- Arranging for the Office of the City Auditor to conduct an in-depth audit of the investment area. This is in addition to the regular audit of the investment area by the City's external auditor. This audit was requested to identify areas for improvement and confirm that the City's investments are managed in a prudent and responsible manner.
- Recommending changes, as directed by City Council, to the dividend formula for the Ed Tel Endowment Fund.

The Investment Committee will continue to monitor and evaluate the effectiveness of the City's investment program and recommend changes where required.

Investment Management

External Fund Management

The Reserves Fund, Ed Tel Endowment Fund and the Pension Funds share the same external investment managers.

Fund Managers:

Canadian Equity
- AMI Partners Inc.
- Greystone Managed Investments Inc.
- TD Asset Management Inc.

Canadian Fixed Income
- Phillips Hager & North Investment Management Ltd.
- Perigee Investment Counsel Inc.
- TD Asset Management Inc.

US Equity
- TD Asset Management Inc.

EAFE Equity
- Lazard Asset Management Inc.
- Fidelity Investments

Internal Fund Management

The Sinking Fund and Working Capital Funds are managed internally by the City of Edmonton Investment Management Section.

The following sections provide details on each of the respective funds

Reserves Fund

Fund Management:
External Investment Managers

Market Value:
$336 Million (Dec. 31, 2002)

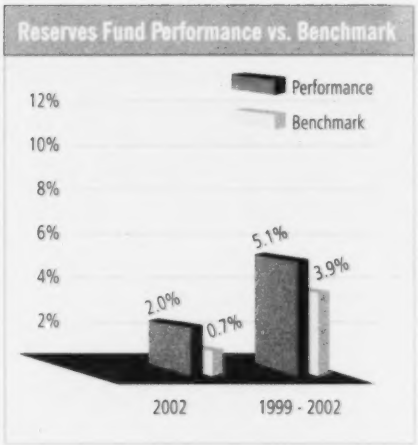
Performance (Rate of Return):

Over one year (2002):	+2.0%
Over four years (1998 - 2002):	+5.1%

Performance against Policy Benchmark:

Over one year:	+1.3%
Over four years (per annum):	+1.2%

Description/Purpose:
Provides an investment vehicle for funds with a long time horizon and a risk tolerance that permits owning equities. Eligible funds include operating and capital reserve funds, deferred revenue accounts, portions of the General Fund and other similarly mandated funds.



Ed Tel Endowment Fund

Fund Management:
External Investment Managers

Market Value:
$561 Million (Dec.31, 2002)

Performance (Rate of Return):

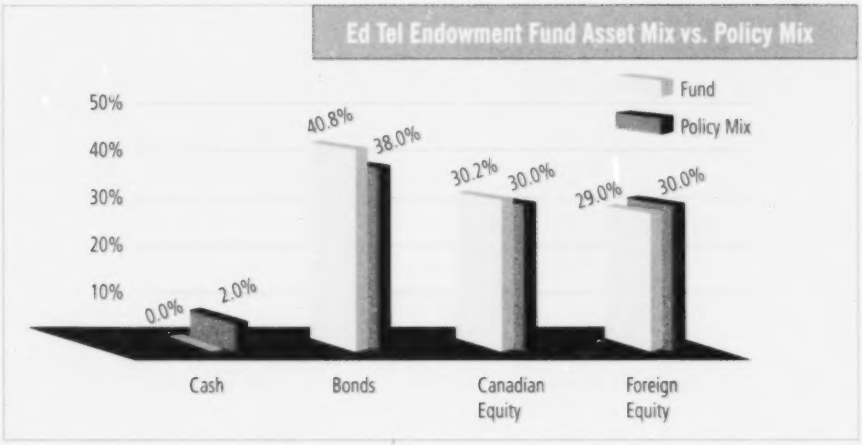
Over one year (2002):	-4.4%
Over four years (1998-2002):	+4.6%

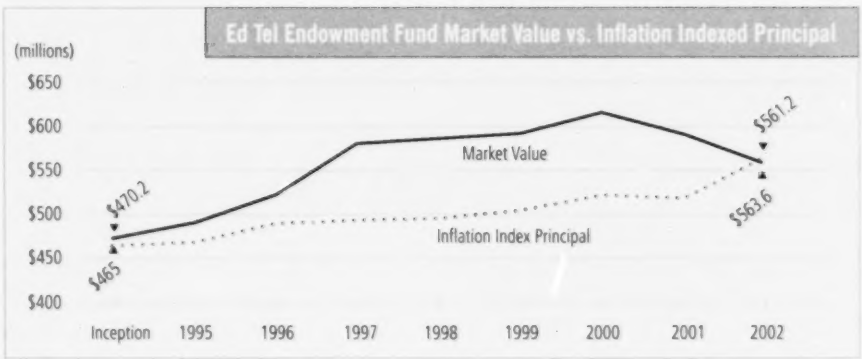
Performance against Policy Benchmark:

Over one year:	+2.6%
Over four years (per annum):	+3.0%

Description/Purpose:
Created in 1995 to hold the financial assets generated by the sale of Edmonton Telephones to the Telus Corporation. The fund's purpose is to provide an income source to the City and to provide a financial legacy for future generations.

Dividend Policy & Fund Bylaw:
The Ed Tel Endowment Fund bylaw governs the process for paying dividends from the Fund. The bylaw requires that the dividend and principal be indexed with the Edmonton Regional Consumer Price Index (CPI). This requirement ensures that the real purchasing power of the fund is maintained for future generations. The Edmonton CPI was 7.9% for the year ending December 31, 2002. The negative investment rate of return combined with a higher than expected inflation adjusted principal precluded a dividend being paid in 2002 for the first time in the eight years since the fund was created. The market value vs. inflation-adjusted principal chart illustrates the reduction of the retained earnings balance over the last two years.

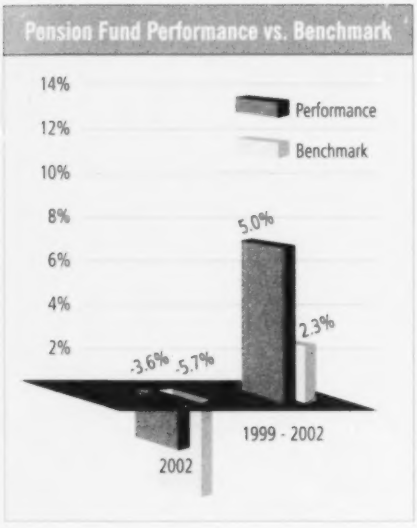


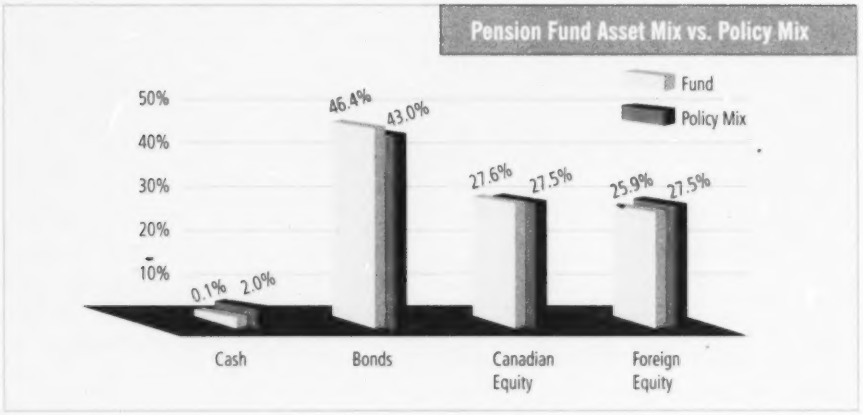


Pension Fund

Fund Management:
External Investment Managers

Market Value:
$107 Million (Dec. 31, 2002)





Performance (Rate of Return):

Over one year (2002):	-3.6%
Over four years (1998-2002):	+5.0%

Performance against Policy Benchmark:

Over one year:	+2.1%
Over four years (per annum):	+2.7%

Description/Purpose:
Consists of the Fire Fighter's Supplementary Pension Plan, the Fire Chiefs' and Deputy Fire Chiefs' Supplementary Pension Plan, and two other small closed pension plans with only a few beneficiaries. Over time the smaller plans will be wound up.

Sinking Fund

Fund Management:
City of Edmonton Investment Management Section (Internal)

Market Value:
$555 Million (Dec. 31, 2002)

Performance (Rate of Return):

Over one year (2002):	+10.6%
Over four years (1998-2002):	+ 6.3%

Performance against Policy Benchmark:

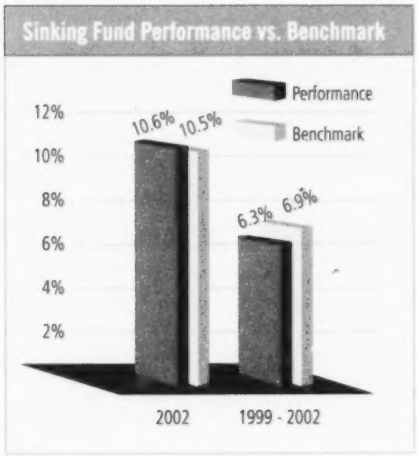
Over one year:	+0.1%
Over four years (per annum):	-0.6%

NOTE: For the year and a half since moving to internal management, the Sinking Fund has returned 12.2% versus 11.9% for the policy benchmark.

Description/Purpose:
The Sinking Fund has existed since the City of Edmonton was incorporated. The fund was established to fulfill the requirement of various public debenture issues (borrowings) requiring funds be set aside regularly for the eventual redemption of these debenture issues. There are currently 13 outstanding debenture issues for which the Sinking Fund is accumulating assets. These debenture issues mature from 2003 to 2018.

Other Information:
In July 2001 the City of Edmonton Investment Management Section assumed responsibility as the fund manager for the Sinking Fund.

At December 31, 2002, the Sinking Fund had a surplus balance of $41 million, after a withdrawal of $37.7 million during 2002. The surplus balance is split between the City and EPCOR, $30.7 million belongs to the City, and $10.3 million to EPCOR. All future surplus earnings will be split 50:50 between the City and EPCOR. Currently, $17.6 million is budgeted to transfer to the City's operating funds over the next two years.



Working Capital Funds

General Fund

Fund Management:
City of Edmonton Investment Management Section (Internal)

Market Value:
$111 Million (Dec. 31, 2002)
The City's significant revenue streams are cyclical, and the fund reaches a peak each July of approximately $375 million.

Performance (Rate of Return):

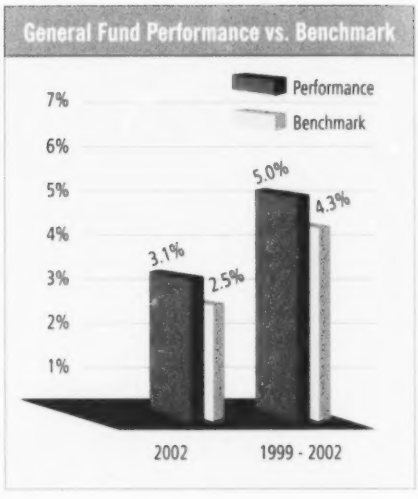
Over one year (2002):	+3.1%
Over four years (1998-2002):	+5.0%

Performance against Policy Benchmark:

Over one year:	+0.6%
Over four years (per annum):	+0.7%

Description/Purpose:
Represents the excess or shortfall in the daily operating funding requirements of the City. The purpose of the fund is to ensure that sufficient cash and liquid assets are available to cover the City's short term obligations.

Other Information:
The duration of the General Fund was shortened in the second half of 2002 by divesting bond holdings totaling $105 million. The proceeds were invested in short term money market instruments to reduce the fund's exposure to a rising interest rate environment. This strategy contributed to the outperformance of the fund.



Transportation Fund

Fund Management:
City of Edmonton Investment Management Section (Internal)

Market Value:
$102 Million (Dec. 31, 2002)

Performance (Rate of Return):

Over one year (2002):	+3.4%
Since Inception (Mar/00 - Dec/02):	+6.0%

Performance against Policy Benchmark:
Comparing against the 4.75% discount rate applied to the initial deposits to the fund indicates that the investment earnings have exceeded the discount rate (6.0% vs. 4.75%).

Description/Purpose:
The Transportation Fund was established in March 2000 with the receipt of fuel tax grants from the Province of Alberta. The agreement with the Province stipulates that the funds:

- be used for approved projects,
- are kept separate from other City funds, and
- that the investment earnings are kept in the fund and applied to approved projects.

Initially, $130 million was received on March 31, 2000 and an additional $52.7 million on June 30, 2000. These original deposits were discounted at a rate of 4.75% in exchange for providing the grant money in advance. These deposits represent an estimate of the fuel grants from April 1, 2000 to March 31, 2003. A further $45 million was received from the Province on March 31, 2002.

Ed Tel Defeasance Fund

Fund Management:
City of Edmonton Investment Management Section (Internal)

Market Value:
$16 Million (Dec.31, 2002)

Performance (Rate of Return):
The performance objective is to generate sufficient returns to repay the outstanding Edmonton Telephones debt. The fund is on target to generate sufficient funds and a surplus of approximately $100,000.

Description/Purpose:
Created in December 1999 when the Telus Corporation paid the outstanding Edmonton Telephones debt in kind by using a portfolio of bonds. These bonds mature at the same time as the City's outstanding debt comes due. The final payment from the fund is on November 1, 2004.

This fund was created solely for the purpose of retiring the outstanding Edmonton Telephones debt. There is very little activity in this fund except on the rare occasions where it is possible to replace existing securities with ones that provide a higher yield while maintaining the same term to maturity.

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EPCOR – *An Investor's Perspective*

To evaluate EPCOR from an "investor's" perspective, the Investment Committee looks for good governance, financial performance and risk management.

Governance

As indicated in the Governance Report Card on the right, the City has established an excellent system of accountability checks and balances.

Financial Performance

A comparison between EPCOR and its peer utility companies (see right) demonstrates that as an investment EPCOR has performed well for the City.

EPCOR is in 2nd place behind Ontario Power Generation, in terms of assets. It is also in 1st place in Net Income and 2nd place behind TransAlta in terms of Return on Equity. While Net Income for full year 2002 of $184 million, is down from $227 million in 2001, this is a result of significantly lower energy prices in 2002. EPCOR's Debt Level is the highest of its peers, at 61%, however including perpetual preferred shares, it is reduced to 55%.

Risk Management

As outlined in the table below, most risks for EPCOR are higher due to deregulation, and the company's expansion into new product markets and regulatory jurisdictions. EPCOR makes good use of the available risk mitigation strategies.

Canadian Energy Companies – Financial Information and Ratio Analysis

Company	Total Assets	Debt Level	Net Income	ROE
Aquila-BC	$429	55.6%	$19	11.7%
Cdn Utilities	$3,737	55.0%	$162	12.3%
EPCOR	**$4,634**	**61.0%**	**$196**	**15.6%**
Great Lakes Power	$3,430	47.1%	$137	11.3%
Nova Scotia Power	$2,860	58.9%	$87	8.9%
Ontario Power Gen	$17,008	38.3%	$63	1.2%
TransAlta Utilities	$3,676	54.7%	$142	16.0%
Group Average	**$5,110**	**52.9%**	**$115**	**11.0%**
*All 12 months ending September 2002				
EPCOR – 2002	**$4,720**	**61.0%**	**$184**	**14.2%**

Governance Report Card

Board of Directors operate independent of City Council	✓
Chairman independent of company executive	✓
Audit Committee controlled by outside directors	✓
Corporation has a Governance Committee and Policy	✓
Board of Directors focused on maximizing shareholder wealth as well as identifying and controlling risks	✓
Corporation is committed to environmental responsibility	✓
Shareholder sets dividend policy	✓

Risk Category	Risk Mitigation	Status
Credit Risk – Customer, supplier or counterparty may default.	Require cash deposits for retailers. Credit worthy or credit support.	✓ May emerge
Operational Risk – Accidents.	Good operating practices.	✓ No change
Merchant Generation – Investing in unregulated generation.	Balance regulated, merchant, contracted and uncontracted.	✓ Emerging as new merchant generators begin production.
Energy Price Risk – Depends on % merchant, % uncontracted, the "hedge ratio" and fuel contracts.	Balance regulated, merchant, contracted and uncontracted. Constrain hedge ratio.	✓ Emerging as new merchant generators begin production.
Market Share Risk – Aggressive new competitors may erode significant market share.	Provide contract terms and administration service levels at or better than any competitor. Counter competitor initiatives.	✓ EPCOR has customer tolls, settlement and billing initiatives underway. ✓ May emerge.
Capital Market Risk – Debt or equity markets may close.	Keep financial ratios consistent with debt rating agencies' targets. Raise both debt and equity.	✓ No change ✓ Equity markets not available at present.
Government and Regulatory Risk – Government can change the regulatory regime or rules.	Use multiple jurisdictions. Strategize around governmental "concerns."	✓ Up – Ontario government has not yet determined its regulatory model.
Overall – Deregulation and business expansion has increased risk.	EPCOR makes good use of the available risk mitigation strategies.	✓ Up

Final Remarks

EPCOR has good governance and has performed well financially for the year 2002. While EPCOR appears to be managing it risks fairly well, the risks have increased due to deregulation and corporate expansion strategies.

Responsible Proxy Voting

- Owning common stock confers certain rights. These include the right to propose and vote on corporate policies through the shareholder resolution process (proxy voting).
- All of the City's proxy votes were cast in accordance with the City of Edmonton Investment Policy C212B. A proxy voting agent is retained to vote the City's ballots for the hundreds of companies in which the City owns shares. The voting service implements the City's policy through careful analysis of each voting issue. During 2002, the City of Edmonton exercised its shareholder rights and voted proxies on 1,015 different corporate resolutions. There were 13 resolutions on social/ethical issues with companies that the City owned shares. The City's proxy votes were cast in support of all of these resolutions. While none of these resolutions were passed, the pressure from shareholders has in many cases positively influenced the companies to change their business practices. For example, shareholder groups withdrew several shareholder resolutions (related to money laundering and employee equal opportunity issues) before they were voted on because the companies preemptively changed their business practices. The pressure from the shareholders and the possibility of the resolutions being passed forced the companies to act. The situation with Talisman Energy is also an example of the effectiveness of shareholder activism. Talisman recently completed the sale of its controversial assets in Sudan after continued pressure from shareholder groups at the company's annual meetings and other venues.

Compliance

A key role of the Investment Committee is ensuring that the City's investments are managed in compliance with the City's investment policy and all relevant legislation.

All of the investment activities of the City's funds were in compliance with the City's policies and all statutory requirements.

Responsibilities of City Council

The role of City Council as governing fiduciaries is to periodically receive reports and recommendations from the City Manager and approve the Investment Policy.

The Investment Policy establishes each fund's:

- investment objectives
- investment beliefs
- permitted investment categories
- asset allocation (policy mix and permitted ranges)
- performance benchmarks
- allowable implementation strategies
- proxy voting guidelines
- monitoring and controls
- reporting requirements

The Investment Committee

The Investment Committee was established by the City Manager to oversee the investment of the City's financial assets.

The roles and responsibilities are clearly defined in the Investment Committee Terms of Reference. The key responsibilities are to:

- Review the Investment Policy and Terms of Reference and recommend changes as necessary.
- Review investment strategies, capital market assumptions, manager structure, services of external managers and other consultants.
- Monitor all reported investment activities for compliance with City policy and statutory requirements.
- Meet with external investment managers, performance measurement advisors, auditors and other consultants as required.
- Monitor investment performance vs. established performance benchmarks.
- Monitor proxy voting activity.
- Review reports on the performance of EPCOR from an investor's perspective.
- Assist the Chief Financial Officer in preparing an annual report on investment performance and compliance for recommendation to the City Manager and City Council.

Investment Committee

Randy Garvey *Chairperson*
Ernie Mulyk *Secretary*
Peter Crosman
Emilian Groch
Bob Grose
Blake Walker
Beverly Wittmack

THE CITY OF Edmonton